Cc: Douglas, Stephen H.; Blumenthal, Jeff; Clark, Morris
Subject: Repatriation of Cash from Enron Canada

Joe,

This note follows up on our conversations last week regarding Enron's ability to repatriate cash from Enron Canada Corp. ("Enron Canada") via repayment of the preferred shares that were issued pursuant to Project Slapshot. As you may recall, as part of the overall Project Slapshot funding, Enron Corp. made a $1.039B capital contribution to Enron Canada ("Capital Contribution") in exchange for the receipt of certain preferred shares ("Preferred Shares"). You have expressed a desire to repatriate cash from Enron Canada by redeeming a portion of the Preferred Shares before the end of the year. However, before deciding whether or not to redeem the Preferred Shares, I thought it would be helpful to provide you with a brief overview of our concerns from a tax perspective.

As you are aware, Project Slapshot conferred significant tax benefits to Enron in the form of an interest deduction by Enron Canada Power Corp. ("ECPC") - such interest deduction is a "permanent" tax difference at the Enron Corp. level (there is no corresponding book accounting deduction) which positively impacts Enron's earnings per share computation by approximately $120MM over the life of Project Slapshot (5 years). In addition, Project Slapshot also created a significant upfront deduction for Enron Canada through the contract termination payments that were made to Enron North America ("ENA") - however, unlike the benefit with respect to the interest deduction, the termination payment deduction is just a "timing" benefit as the deduction will reverse itself over time.

By way of background, our Canadian tax analysis with respect to these Project Slapshot benefits is predicated on two significant factors: (i) Enron Canada has a legitimate business purpose for receiving the Capital Contribution from Enron (and, similarly, ECPC has a legitimate business purpose for borrowing the $1B from Stadacona/EIM); and (ii) Enron Canada did not have a tax-avoidance motive for entering into Project Slapshot.

It should be noted that repaying the Preferred Shares within the same year as entering into Project Slapshot puts pressure on both of the above factors and, as such, puts the integrity of the transaction at risk. For instance, any business purpose that we can articulate with respect to the Capital Contribution (*ie*. ECC's capital structure needed to be revised so as to ensure the ability to obtain future capital/trading capacity on a stand alone basis) loses substance if the capital is returned within the same year that the transaction was entered into. Furthermore, our argument that Project Slapshot does not create any incremental "tax" benefit as compared to a more traditional financing becomes suspect if we are able to immediately move cash across the border on a tax-free basis (a traditional financing does not confer such a tax benefit -- which seems to highlight a potential tax motivation for entering into the financing through the more complex Project Slapshot structure). Thus, while it is uncertain whether the current repayment of the Preferred Shares will ultimately prove fatal to our tax analysis, it is certainly our position that the greater the period of time that we can interpose before repaying any of the Preferred Shares, the greater the likelihood of withstanding an attack by Revenue Canada on audit.

While we can appreciate the importance of the commercial realities of managing Enron's overall cash position, I just wanted to make sure that you understood the tax implications of repaying the Preferred Shares this year so that you can be "armed" with all of the facts when assessing Enron's needs from a cash management perspective. As is always the case, once you have had a chance to digest the tax risks outlined above, I would be happy to discuss with you in greater detail.